

UNITED STATES DISTRICT COURT
DISTRICT OF MAINE

In re CATHERINE DUFFY PETIT,
Plaintiff

CATHERINE DUFFY PETIT,
Debtor/Appellant

v.

JOSEPH V. O'DONNELL,
Trustee/Appellee

Bankruptcy Appeal
No. 96-CV-149-P-C

Bankruptcy Case
No. 93-20821

GENE CARTER, District Judge

MEMORANDUM OF DECISION AND ORDER
GRANTING APPELLEE'S MOTION TO DISMISS APPEAL

Debtor Catherine Duffy Petit ("Debtor" and "Appellant" herein) appeals from a judgment and order of the United States Bankruptcy Court for the District of Maine, dated January 17, 1996, granting the application of Trustee Joseph V. O'Donnell ("Trustee" and "Appellee") to employ Stephen G. Morrell, Esquire, and the law firm Eaton, Peabody, Bradford & Veague, P.A. ("Eaton, Peabody") as general counsel. Now before the Court are Debtor's Appeal from Judgment and Order of the Bankruptcy Court Granting Trustee's Application (Docket Nos. 1 & 2) and Trustee's Motion to Dismiss Appeal (Docket No. 4). The Court concludes, for the reasons stated below, that the issues raised on appeal are moot and the appeal, therefore, will be dismissed.

I. FACTS

This case commenced on June 4, 1993, with the filing of an involuntary petition against Debtor, pursuant to Chapter 7 of the United States Bankruptcy Code, in the United States Bankruptcy Court in the District of Maine. Docket Sheet (Volume I-12), at 3. The case was converted to an action under Chapter 11 and subsequently converted back to Chapter 7. Id. at 8, 36. On December 11, 1995, Joseph O'Donnell was appointed Trustee, replacing former Trustee Peter Fessenden. Id. at 32. On December 26, 1995, the Trustee filed an application to employ Stephen G. Morrell, Esquire, of the law firm Eaton, Peabody, as general counsel to the Trustee. Application for Approval of Employment of Attorney (Volume I-2). The reason for this appointment was to assist the Trustee in responding in a timely manner to a series of pending motions to dismiss relating to adversary proceedings commenced by Fessenden. Brief of Appellee at 5.

In connection with the Trustee's application, Morrell filed an Attorney Affidavit, which stated that:

To the best of my knowledge, neither I nor any member or associate of the firm of [Eaton, Peabody] represents any interest adverse to the Debtor, other than an award of fees in the previous Chapter 7 case ordered by this Court on April 28, 1995. Further, we are a disinterested party with respect to the Debtor.

To the best of my knowledge, there are no connections of the firm and myself with the

Debtor, creditors, any other parties in interest, their respective attorneys and accountants, the United States Trustee, and persons employed in the office of the United States Trustee, with one exception:

[Eaton, Peabody] represents the law firm of [Bernstein, Shur] in a civil action pending in the United States District Court for the District of Maine entitled Penobscot Indian Nation v. Key Bank of Maine, et al, Civil Action No. 94-212-B. . . . The attorneys representing the Penobscot Indian Nation are counsel of record to the Debtor in this case. It has been suggested by counsel that this firm's connection with [Bernstein, Shur] in that case is adverse to the estate in this case. The undersigned has investigated the matter with the Trustee and considers the fact that the Debtor released [Bernstein, Shur] of all claims for a valuable consideration, prepetition, to render immaterial this firm's connection to [Bernstein, Shur] for purposes of this engagement.

Attorney Affidavit (Volume I-3) ¶¶ 4, 5. On January 4, 1996, Bankruptcy Judge Votolato conducted a telephone hearing on the Trustee's application, in which the Trustee, Stephen Morrell, and Gerrard Kelley, Esquire, the United States Trustee, participated. Transcript of Hearing (Volume I-5). Debtor and Debtor's counsel did not participate in, or have notice of, the hearing.¹ Id.; see also Brief of Appellant at 8. Judge Votolato acknowledged

¹Morrell attested by Certificate of Service, dated December 22, 1995, that he had forwarded a copy of the application and attorney affidavit, as well as a proposed order, by mail to Stephen F. Gordon, Esquire, counsel to the Debtor. Certificate of Service, attached to Debtor's Objection to Application (Volume I-4) as Exhibit A. However, Debtor claims that "Debtor's counsel was never served with a copy of the employment application until 4:00 p.m. on January 8, 1996 . . . by facsimile. . . ." Brief of Appellant at 7. Debtor also asserts that Debtor's counsel received no notice of the hearing that took place on January 4. Id. at 8.

that the Debtor was "intentionally not included" in the hearing. Transcript at 4, line 5.

Debtor filed an objection to the application to employ Morrell, dated January 4, 1996, challenging the application on the grounds that, inter alia, Morrell and/or Eaton, Peabody had a conflict of interest with the Debtor's estate. Debtor's Objection to Application (Volume I-4). Specifically, the Debtor maintained that Eaton, Peabody's representation of Bernstein, Shur, Sawyer & Nelson ("Bernstein, Shur") in Penobscot Indian Nation v. Key Bank of Maine, et al, Civil No. 94-212-B, ("Penobscot litigation") constituted representation of an interest adverse to the Debtor's estate. Id. Debtor alleged that she had a meritorious claim against Bernstein, Shur for making a settlement agreement in 1990 with the Debtor ("settlement")² which constituted a fraudulent transfer,³ and that Eaton, Peabody's ongoing representation of her estate's

²The settlement consisted of an agreement by the Debtor to release Bernstein, Shur of legal claims in exchange for approximately \$3.8 million (a sum which has been alternately cited in the pleadings as \$3.8 million, \$3.9 million, and \$4 million). Brief of Appellant at 9, 15.

³On appeal, Debtor makes the additional argument that Morrell and Eaton, Peabody should be disqualified on the basis of an actual conflict of interest with Debtor's estate. Brief of Appellant at 9, 16. In support of this contention, Debtor alleges that she has been "falsely accused by Eaton, Peabody (in an effort to aid Bernstein, Shur's defense of the Penobscot Indian Litigation) of having an undisclosed interest in the Penobscot Indian Litigation." Opposition to Motion to Dismiss ¶ 9. The Court will address this issue in the "Discussion" section, infra.

potential adversary should preclude Morrell from serving as counsel to the Trustee. Id.

Anticipating that the bankruptcy judge would grant the Trustee's application, Debtor filed a motion to reconsider, dated January 12, 1996 (Volume I-6). On January 17, 1996, Judge Votolato issued a Judgment and Order finding no present conflict of interest, granting Trustee's application to employ Morrell, and denying Debtor's Motion for Reconsideration (Volume I-7). In addition, Judge Votolato's order stated that "to ensure that all matters involving Bernstein, Shur, Sawyer & Nelson are properly and fully investigated, the Trustee has agreed, and the Court has ordered that the Trustee hire special, independent counsel to investigate, and to prosecute, if appropriate, all Bernstein, Shur matters." Order (Volume I-7), at 1-2. From this order, Debtor appeals. Notice of Appeal (Volume I-8).

In February 1996, the bankruptcy court authorized Steven E. Cope, Esquire, to represent the Trustee as counsel for the special purpose of investigating whether the estate had any legal claims against Bernstein, Shur, and whether Bernstein, Shur held any interest in the Debtor's bankruptcy case. Affidavit of Steven E. Cope, Esquire (Docket No. 5). On June 27, 1996, special counsel issued a report of his investigation, which concluded that, "the Trustee, in good faith, determined that there was insufficient merit to proceed with an avoidance action [pursuant to the Maine Uniform Fraudulent Transfer Act] and took no action by the expiration of the deadlines set forth in 11

U.S.C. § 546." Report of Special Counsel, attached to Trustee's Reply Memorandum (Docket No. 7) as Exhibit A, at 11. In addition, Cope has stated that "[Bernstein, Shur] holds no claim against the [Debtor's] estate . . . [and] I have no knowledge of any other claim of the estate against [Bernstein, Shur]." Affidavit of Steven E. Cope, Esq. (Docket No. 5).

II. DISCUSSION

On appeal, Debtor argues that the bankruptcy court erred in granting the application to employ Morrell as general counsel to the Trustee.⁴ The Trustee makes a number of counter arguments, but nonetheless moves to dismiss on the ground that the issues raised on appeal are now moot. Motion to Dismiss (Docket No. 4). The Court agrees with the Trustee. It is unnecessary, and indeed

⁴The Debtor alleges that the bankruptcy judge made a series of other errors as well: (1) holding a hearing without notice to the Debtor, (2) granting an application in which the accompanying attorney affidavit did not adequately disclose the nature of the conflict, and (3) ordering the Trustee to hire special counsel. Brief of Appellant at 4-5.

Even assuming that the bankruptcy judge made those errors, the remedy that the Debtor seeks is the same: a reversal of the bankruptcy court's order granting the application. The Court therefore focuses its inquiry here on the Debtor's two central allegations: namely, the bankruptcy court's finding of no actual conflict of interest and its determination that the Penobscot litigation was "unrelated" to the Debtor's case. Because the Court concludes that these central issues are moot, allegations (1) and (2), which pertain to procedural fairness, are also moot. Moreover, the Court assumes that even though the Debtor did not participate in the telephone hearing on the Trustee's application, the bankruptcy court had the opportunity to consider the Debtor's brief before issuing its Order approving the employment of Morrell and Eaton, Peabody. The Court addresses allegation (3) in footnote 6, infra.

it would be inappropriate, for this Court to rule on whether the bankruptcy court erred, since the legal issues raised on appeal have been rendered moot by the subsequent findings of special counsel Stephen E. Cope.

Mootness

As this Court recognized in Bank of New England v. BWL, Inc., 121 B.R. 413 (D. Me. 1990), Article III limits the jurisdiction of federal courts to matters in which there is a "case or controversy": "[A] plaintiff must demonstrate that he is suffering a concrete and direct injury, or the danger that such injury is posed by a real and immediate threat, before a federal court may assume jurisdiction." Id. at 416, citing Linda R.S. v. Richard D., 410 U.S. 614, 617 (1973). Not only is a plaintiff required to show injury, but the injury "must survive throughout the course of a litigation." Id. Indeed, when developments during the course of the lawsuit, in effect, deprive the court of its ability to redress the injury, then the case becomes moot, and the court no longer has jurisdiction. Id. It is important to note, further, that "[t]his constitutional mandate to refrain from issuing advisory opinions on moot questions is no less effective in bankruptcy cases." Id.

As stated above, Debtor's central argument on appeal is that the bankruptcy court erred in granting the application to employ Morrell as general counsel to the Trustee. The remedy Debtor seeks from this Court is reversal of the bankruptcy judge's order

granting the Trustee's application to employ Morrell. Debtor renews this request in her objection to the Trustee's motion to dismiss, stating that "reversal of the Employment Order is a grant of relief and would permit the engagement of qualified, independent, unconflicted counsel for the Trustee." Objection to Motion to Dismiss ¶ 14, p.5. In light of the report of special counsel, and for the reasons outlined below, this Court is convinced that there is no existing injury to the Debtor which requires a remedy.

Debtor asserts that there are two separate sources of a conflict of interest which disqualify Morrell from serving as the Trustee's general counsel: (1) Morrell and Eaton, Peabody represent an interest adverse to her estate and are not "disinterested persons," since her estate had a potential claim against Eaton, Peabody's client, Bernstein, Shur, under the Maine Uniform Fraudulent Transfer Act ("MUFTA"), and (2) Eaton, Peabody has an actual conflict of interest with the Debtor since it made false allegations that the Debtor's estate had an undisclosed interest in the Penobscot Indian litigation.

1. Representation of an "adverse interest":

Debtor argues that Morrell does not meet the requirements for appointment of general counsel to the Trustee, as set forth in 11 U.S.C. § 327(a), and the definition of "disinterested

person," as defined in 11 U.S.C. § 101(14).⁵ Specifically, Debtor maintains that at the time of Trustee's application to employ Morrell, Debtor's estate had a meritorious legal claim against Bernstein, Shur under MUFTA. Brief of Appellant at 15. According to Debtor, Bernstein, Shur's exchange of nearly \$4 million for Debtor's release of legal claims in 1990 was an exchange for inadequate consideration, and was made with "actual intent to hinder, delay, or defraud the Debtor's creditors," in violation of MUFTA. Opposition to Motion to Dismiss ¶ 9 at 3. In addition, Debtor contends that at the time of the application to employ Morrell, the possibility of such a claim was "inconclusively investigated." Brief of Appellant at 15. Given the potential claim, Debtor argues, the bankruptcy court erred in approving the employment of Morrell, since a partner of Morrell's at Eaton, Peabody was acting as counsel to Bernstein, Shur in the Penobscot litigation.

The Trustee asserts that the bankruptcy judge properly took into account the concerns of the Debtor by ordering the Trustee to hire special counsel to assist in investigating the Debtor's

⁵11 U.S.C § 346 states that "the trustee, with the court's approval, may employ one or more attorneys . . . that do not hold or represent an interest adverse to the estate, and that are disinterested persons, to represent or assist the trustee in carrying out the trustee's duties under this title."

To qualify as a "disinterested person," as defined in 11 U.S.C. § 101, one must not "have an interest materially adverse to the interest of the estate or of any class of creditors or equity security holders, by reason of any direct or indirect relationship to, connection with, or interest in, the debtor . . . for any other reason."

alleged claim under MUFTA. Notwithstanding Debtor's repeated contention that the bankruptcy judge did not afford her adequate opportunity to be heard, this Court is persuaded that Judge Votolato sought to avert a conflict, as reflected by his decision to order a full investigation⁶ of the Debtor's potential legal claims against Bernstein, Shur and Bernstein, Shur's potential interest in the Debtor's bankruptcy case.

After completing an investigation, special counsel Cope issued a report in which he concluded that the Debtor's asserted fraudulent transfer claim against Bernstein, Shur was not actionable.⁷ The Court concludes that it is bound by special counsel Cope's findings regarding the actionability of the Debtor's allegations against Bernstein, Shur because the validity of the special counsel's report and findings have never been challenged by the Debtor. The Debtor's response to Trustee's

⁶As indicated above, Judge Votolato simultaneously granted the application to employ Morrell and Eaton, Peabody as general counsel, and ordered the Trustee to hire special counsel to investigate the Debtor's relationship with Bernstein, Shur, if any. The Bankruptcy Code authorizes the appointment of what the Court has designated here as general and special counsel. See 11 U.S.C. § 327(a) & (e). While a better course may have been to condition the employment of Morrell upon the outcome of the investigation, this Court is satisfied, based upon the record before the Court, that the Debtor has not been prejudiced by the bankruptcy judge's decision.

⁷The Court notes that after careful examination of the Trustee's Motion to Dismiss (Docket No. 4) and the Affidavit of Steven Cope (Docket No. 5), it is not clear when Cope arrived at this conclusion. The Court relies on the special counsel's findings as set forth in his report of June 27, 1996, but notes that the statute of limitations for bringing an avoidance claim apparently ran on June 9, 1996. The Court addresses the statute of limitations issue at greater length infra.

Motion to Dismiss neither takes issue with the specific content of the report nor alleges that Cope engaged in any impropriety in preparing the report. See Debtor's Opposition to Motion to Dismiss (Docket No. 6). Furthermore, the Court concludes that special counsel Cope's report renders the Debtor's appeal moot.

The Debtor insists that the controversy in this case -- namely, the alleged conflict of interest -- still "survives" at this point in the litigation, notwithstanding the findings of the special counsel. However, the Trustee asserts, and Debtor does not dispute, that the statute of limitations for commencing an action ran on June 9, 1996. The fraudulent transfer claim being time-barred, the Debtor is legally unable to bring the action which, Debtor alleges, forms the basis for a potential conflict of interest.⁸

2. Actual Conflict

The Debtor alleges that Morrell and Eaton, Peabody have an actual conflict of interest with the Debtor insofar as Eaton, Peabody has made false allegations both in the bankruptcy court and in the United States District Court that the Debtor's estate

⁸As the Court noted in Bank of New England, supra, "these eggs cannot be unscrambled." 121 B.R. 413, 417. While the Debtor asserts in pleadings that the Trustee's decision to refrain from bringing an avoidance action may give rise to some other action for "neglect and failure of the Trustee to bring that claim," see Opposition to Motion to Dismiss at 3, the Court notes that any such action pertains to the adequacy of the Trustee's performance of his duties, and is unrelated to the matter before this Court -- that is, the alleged conflict of interest of Trustee's general counsel.

has an undisclosed interest in the Penobscot litigation. Opposition to Motion to Dismiss ¶ 9 at 3. Although this issue is mentioned in passing in Cope's report, it appears that it was not formally investigated. The Debtor asserts that "actual conflicts, as well as the negative appearances therefrom, still exist and pose continuing harm to the creditors and the entire estate." Opposition to Motion to Dismiss (Docket No. 6) at 5.

The Court finds this argument wholly unpersuasive, as the Debtor raises it fleetingly and fails to develop it coherently. The Debtor attempts to use rumors of her undisclosed interest in the Penobscot litigation as a basis for alleging an actual conflict of interest, while simultaneously denying that she has such an interest. To the extent that the Debtor repeatedly disavows any interest in the Penobscot litigation,⁹ she cannot use such allegations to exemplify a conflict and thereby avoid Trustee's employment of attorney Morrell.

III. CONCLUSION

The Court concludes that the report of special counsel lays to rest the issue of a conflict of interest by demonstrating that Debtor had no meritorious claim against Bernstein, Shur. Thus, Morrell and Eaton, Peabody do not represent an interest adverse to the Debtor's estate, and Morrell does qualify as a

⁹Debtor asserts that she has been " . . . falsely accused (in an effort to aid Bernstein, Shur's defense of the Penobscot Indian Litigation) of having an undisclosed interest in the Penobscot Indian Litigation." Brief of Appellant at 9.

"disinterested person" under 11 U.S.C. § 101(14). There being no remedy available to the Debtor that this Court can issue, in view of the Cope report, the Court finds that the issues raised on appeal are moot, and the Court lacks jurisdiction to render an opinion on the appeal.

Accordingly, the Court GRANTS the Trustee's Motion to Dismiss the appeal, and the appeal of the Judgment and Order of the bankruptcy court is hereby DISMISSED.

So ORDERED.

GENE CARTER
District Judge

Dated at Portland, Maine this 27th day of January, 1997.